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UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF CALIFORNIA

In re

CHAD E. PERTH, and
NENITA PERTH,

Debtors. /

CHAD E. PERTH, and
NENITA PERTH,

Plaintiffs,

vs.

TEXAS GUARANTEED STUDENT LOAN
CORPORATION,

Defendant. /

DECISION

By this adversary proceeding, plaintiffs Chad E. Perth ("Chad") and Nenita Perth ("Nenita"), the above debtors, seek to discharge their student loan debts owing to defendant Texas Guaranteed Student Loan Corporation ("Texas"), on the grounds that repayment would

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Decision

1 impose an "undue hardship" within the meaning of Bankruptcy Code
2 § 523(a)(8)(B)¹.

3 The debt at issue (the "Debt") is in the principal sum of
4 \$45,791, which amount accrues interest at the annual rate of 9%,
5 plus past due accrued interest in the sum of \$17,845 (as of
6

7 ¹Bankruptcy Code § 523(a)(8) has been amended for
8 bankruptcy cases filed after October 7, 1998. Higher
9 Education Amendments of 1998, P.L. No. 105-244, 112 Stat. 1581
10 (1998). Section 523(a)(8)(B), as in effect for cases filed
on or before October 7, 1998, provides:

11 (a) A discharge under section 727 . . . of this title
12 does not discharge an individual debtor from any debt—

13

14 (8) for an educational benefit overpayment or loan made,
15 insured or guaranteed by a governmental unit, or made under
16 any program funded in whole or in part by a governmental unit
17 or non-profit institution, or for an obligation to repay funds
18 received as an educational benefit, scholarship or stipend,
unless—

19

20 (B) excepting such debt from discharge under this
21 paragraph will impose an undue hardship on the debtor
22 and the debtor's dependents; . . .

23 All further section references herein are to the United States
24 Bankruptcy Code, 11 USC § 101 et. seq., as in effect for cases
25 filed on or before October 7, 1998.
26

1 September 1998), for a total debt of \$63,636. The court holds
2 that the Debt is dischargeable herein.

3 The parties agree that although the Bankruptcy Code does not
4 define "undue hardship", the meaning of the term is governed by
5 the ninth circuit's decision in In re Pena, 155 F.3d 1108 (9th
6 Cir. 1998). Pena adopted the three-part test articulated in In re
7 Brunner, 46 B.R. 752, 753 (S.D.N.Y. 1985), aff'd, 831 F.2d 395 (2d
8 Cir. 1987). Pena, 155 F.3d at 1114. Under this test, the debtor
9 must first establish that she:

10 cannot maintain, based on current income and expenses, a
11 'minimal' standard of living for herself and her
12 dependents if forced to repay the loans.

13 Pena, 155 F.3d at 1111 (quoting Brunner, 831 F.2d at 396).

14 Next, the debtor must show that "additional circumstances
15 exist indicating that this state of affairs is likely to persist
16 for a significant portion of the repayment period of the student
17 loans." Id. Finally, the debtor must have made "good faith
18 efforts to repay the loans." Id.

19 A. Minimal Standard of Living Test

20 The first issue is whether the debtors could maintain a
21 "minimal" standard of living for themselves and their dependents
22 if they were forced to repay the Debt. Pena, 155 F.3d at 1111.
23 In applying this test, the court may not grant a partial discharge
24 of the Debt, even if the court were to find that some partial
25 payment might be feasible. In re Taylor, 223 B.R. 747 (9th Cir.
26 BAP 1998); see also In re Brown, 227 B.R. 540, 547-48 (Bankr. S.D.

1 Cal. 1998).

2
3 Here, the evidence was in conflict as to whether the debtors'
4 income and expenses would permit them to repay any portion of the
5 Debt. The debtors live with three children, whose ages are 5, 8,
6 and 22. A fourth child, age 14, requires special care, and lives
7 at a boarding school. Chad is responsible for supporting two
8 additional children, ages 11 and 14, who reside in San Bernardino
9 County. Chad is presently paying the County of San Bernardino the
10 monthly sum of \$406 for their current support, plus an additional
11 \$100 per month to repay a debt in the sum of approximately \$12,000
12 for past due child support. Chad originally owed the County over
13 \$24,000 for child support, but in June 1998, the County agreed to
14 forgive approximately \$12,000 of this support debt, based on
15 Chad's inability to repay it.

16 The debtors incurred the Debt to fund the cost of court
17 reporting school. Chad did not finish his training, and currently
18 works as a computer network administrator. Nenita finished, but
19 was not able to pass the court reporting test after numerous
20 attempts. She is currently employed by the University of
21 California as an administrative assistant.

22 The debtors' schedules I and J show that as of May 12, 1998,
23 the date of their chapter 7 petition, their combined, net monthly
24 income of \$4,304 was not sufficient to meet their scheduled
25 monthly living expenses of \$4,504 (which expense amount does not
26 include any sums for repayment of the Debt).

1 After the petition, the debtors enjoyed an increase in their
2 combined, net monthly income. The most recent pay stubs show that
3 Nenita earns a gross monthly income of \$3,295 and a net monthly
4 income (after deduction of various amounts for taxes, insurance,
5 and payments into a retirement plan) of \$2,530. Chad's recent pay
6 stubs show that he earns a current gross income of \$3,230 and a
7 net income (after deduction of various sums for taxes, insurance,
8 and child support) of \$1,966. Thus, the debtors' current,
9 combined, gross, monthly income is approximately \$6,525.

10 Texas contends that when the expenses that are deducted from
11 the debtors' paychecks are added to the additional expenses that
12 the debtors scheduled, the total is \$5,884, and that the debtors
13 therefore have the monthly sum of \$641 (\$6,525 - \$5,884) or more²
14 available for repayment of the Debt. Texas also contends that
15 some of the debtors' paycheck deductions are for discretionary
16 items such as life insurance and retirement plan payments,
17 totaling, \$250 and \$43 per month, respectively, and that the
18 debtors could use these funds for Debt repayments.

19 The debtors contend that the expense figures they scheduled
20 were minimum, conservative figures, and that they do not have any
21 surplus income to use for Debt repayments. They also contend that
22 their expenses have increased since the date of the filing.

23
24 ²The 22 year old son contributes approximately \$55 per
25 month toward household expenses, which, using Texas's
26 methodology, would increase the debtors' income available for
debt repayment to approximately \$700 per month.

1 Further, debtors claim that their budget in Schedule J makes no
2 allowance for contingencies. For example, the debtors point out
3 that one of the two cars that they need for transportation to and
4 from work is over 13 years old, and paid for, and argue that they
5 will therefore need to finance another car, and pay for additional
6 insurance, in the near future.

7 The court agrees with the debtors. Initially, the court
8 rejects Texas's argument that the debtors' life insurance and
9 retirement contributions should not be considered as valid
10 expenses. The mere fact that they are discretionary, rather than
11 mandatory, does not mean that they are not legitimate expenses for
12 purposes of § 523(a)(8). Moreover, the amounts do not appear to
13 the court to be unreasonable. Finally, five minor children rely
14 on the debtors' income for their support, and the debtors' life
15 insurance contributions therefore appear to be a prudent
16 investment under the circumstances.

17 The court also agrees that the debtors will need to purchase
18 or lease another vehicle, with related insurance, in the near
19 future, which would probably cost them an additional \$250 - \$300
20 per month. Therefore, even if the court were to assume that the
21 debtors' expenses have not risen since the petition date, the
22 debtors would still have only approximately \$400 - \$450 available
23 each month to cover unanticipated emergencies and to repay Debt³.

24
25 ³The debtors' budget states that the family medical
26 expenses are \$30 per month, which would be an average of \$6
(continued...)

1 It follows that even if the debtors will never have an
2 emergency expenditure that is not in their budget, the debtors
3 could not possibly pay off the Debt at the rate of \$400 per month.
4 Interest at 9% per annum on the principal of \$45,791 accrues at
5 the rate of \$4,121 per year. Thus, if the debtors were to pay
6 Texas \$400 per month, principal would only reduce at the rate of
7 \$679 per year ($12 \times \$400 = \$4,800$ per year paid; $\$4,800$ paid -
8 $\$4,121$ annual interest = $\$679$ per year principal reduction). At
9 this rate, the debtors would need over 67 years to repay the
10 principal of \$45,791⁴.

11 The debtors actual prospects for repaying the Debt are
12 probably even worse: if the debtors were to begin payments of \$400
13 per month, and if Texas applied these payments, first to accrued
14 and past due interest, then it would take the debtors some 45
15 months to repay the outstanding past due interest of \$17,845.
16 But, during this 45 months, more than \$15,400 in additional
17 interest would have accrued on the outstanding principal of
18 \$45,791. It would therefore take a very long time before
19 principal reductions would even begin.
20

21 ³(...continued)
22 per person, per month for the five family members in
23 residence. The court has no evidence as to whether the
24 debtors' medical insurance and the additional \$30 per month is
25 sufficient for the family's needs, although the budgeted item
26 seems quite low.

⁴Using a hypothetical payment of \$450 per month results in
\$45,791 being repaid after 36 years.

1 In short, based on presently available information, and the
2 debtors' current financial condition, it would be virtually
3 impossible for the debtors to ever repay the Debt. If the debtors
4 were forced to payoff this Debt within a reasonable time (or for
5 that matter, within their lifetimes), then, they could not
6 maintain a minimal standard of living. The debtors have therefore
7 satisfied the first prong of the Pena test. See In re Brown, 227
8 B.R. 540, 545 (Bankr. S.D.Cal. 1998).

9 B. Condition Likely to Persist

10 Texas next contends that the debtors' ability to repay the
11 Debt will increase as the number of children they must support
12 decreases. Although this may be true, it is also true that the
13 debtors' children will require support for many more years before
14 any increased ability to pay may occur. Of the five minor
15 children that the debtors are currently responsible for
16 supporting, the two youngest children, ages 8 and 5, will
17 presumably reside with the debtors for at least the next ten to
18 thirteen years.

19 Chad's obligation to support the children in San Bernardino
20 County will not completely terminate for at least another seven
21 years. Also, Chad's past due support obligation to the County may
22 continue after his ongoing support obligation ends when the
23 children turn 18.

24 One other additional factor, the future earnings benefit of
25 the education received, also weighs in favor of the debtors.
26 Neither debtor is employed, or appears likely to be employed, as a

1 court reporter. No additional evidence was presented in court
2 indicating that either debtor has a significant likelihood of
3 enjoying increased earnings from other sources that would enable
4 them to repay the Debt.

5 Additional circumstances clearly exist limiting the debtors'
6 ability to make future payments on the Debt. Thus the second
7 prong of the Pena test is satisfied.

8 C. Good Faith

9 Texas next argues that the debtors' failure to make any
10 student loan payments prevents them from satisfying the third
11 prong of the Pena test. The court disagrees.

12 The debtors testified that payments initially became due on
13 the Debt in 1991. Because the debtors were unable to make
14 payments at that time, they requested, and the lender granted, a
15 deferment of the loan payments.⁵ The lender continued granting
16 the debtors' requests for deferment every three to six months
17 until the bankruptcy filing.

18 In Brunner, the court found that the debtor failed to
19 establish good faith because she "filed for discharge within a
20 month of the date for the first payment of her loans came due, . .
21 . . made virtually no attempt to repay, [and never] requested a
22 deferment of payment, a remedy open to those unable to pay because
23 of prolonged unemployment." Pena, 155 F.3d 1114 (quoting Brunner,

25 ⁵Sallie Mae Servicing Corporation, Texas's predecessor as
26 holder of the student loans, granted the deferments.

1 46 B.R. at 758 (alteration in Pena)). In Pena, the court found
2 that the debtors had exhibited good faith where they made some
3 payments, received a 90-day deferment, and then filed bankruptcy.
4 See id.

5 Here, the debtors filed their bankruptcy case approximately
6 seven years after payments first came due. Never having had the
7 means to make any payments, the debtors continually requested and
8 received deferments. The debtors have satisfied the third prong
9 of the Pena test by exhibiting good faith in working with their
10 lender to receive deferments on the student loans, rather than
11 simply defaulting on the payments or filing bankruptcy as soon as
12 they realized that they could not repay the Debt.

13 For the foregoing reasons, the court will issue its judgment
14 discharging the Debt.
15

16 Date: August 19, 1999
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18

19 _____
20 Edward D. Jellen
21 United States Bankruptcy Judge
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